

Message Text

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SUBJECT: JAPANESE RECOVERY NEEDS ADDITIONAL FISCAL STIMULUS, SAYS
BOJ OFFICIAL

1. SUMMARY. ADDITIONAL FISCAL STIMULUS FOR JAPANESE ECONOMY IS BEING URGED BY INCREASINGLY LARGE NUMBERS OF JAPANESE. MANIFESTO ISSUED BY 13 PROMINENT ECONOMISTS INCLUDING SENIOR BANK OF JAPAN ADVISOR SUZUKI CALLS FOR TAX CUT. SUZUKI HAS TOLD EMBASSY EVEN PM MIKI AND BOJ GOV MORINAGA NOW SHARE THAT VIEW BUT ARE UNWILLING TO OVERRIDE FUKUDA'S CONTINUING POLICY OF RESTRAINT. BOJ OFFICIAL DOES NOT ENTIRELY RULE OUT POSSIBILITY THAT PM MIKI WILL CALL FOR INCOME TAX CUT JUST BEFORE LOWER HOUSE ELECTIONS ARE HELD LATER THIS YEAR. END SUMMARY.

2. SENIOR BOJ ADVISOR (YOSHIO SUZUKI) EXPLAINED TO FINATT HIS VIEWS ON CURRENT ECONOMIC POLICY AND OUTLOOK. SUZUKI IS ONE OF PM MIKI'S PERSONAL ADVISORS AND APPARENTLY A MUCH SOUGHT AFTER SPEAKER BY SMALL POLITICAL GROUPS. HE IS KNOWN AS BOJ'S MOST ABLE ECONOMIST TO SOME
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WASHINGTON OFFICIALS AND BROOKINGS STAFF.

3. SUZUKI SAYS HIS OWN VIEWS ARE WIDELY SHARED BY REPUTABLE ACADEMIC ECONOMISTS AS WELL AS SOME EPA OFFICIALS WHO HAVE REACHED SIMILAR CONCLUSIONS. SUZUKI SAID PM MIKI AND BOJ POLICY BOARD NOW ACCEPT THE NEED FOR ADDITIONAL FISCAL STIMULUS TO MOVE THE ECONOMY CLOSER TO ITS POTENTIAL. PM MIKI WOULD LIKE TO ACT BUT LOST HIS OPPORTUNITY AFTER HE WAS FORCED ON TO THE DEFENSIVE AS A RESULT OF DIET IMBROGLIO OVER LOCKHEED ISSUE. GOV MORINAGA BELIEVES BOJ CANNOT TAKE INITIATIVE BUT IS PLAYING SUPPORTIVE ROLE IN MONETARY EXPANSION. EPA STAFF REPORTEDLY HAS "GIVEN UP" TRYING TO EDUCATE DIR GEN FUKUDA OF THE ADVERSE CONSEQUENCES OF HIS PRESENT POLICY. MINFIN OHIRA IS APPARENTLY UNWILLING TO ACT, FOR PERSONAL POLITICAL REASONS (EVEN THOUGH MEMBERS OF HIS POLITICAL FACTION ARE GROWTH-ORIENTED) AND BECAUSE MOF CONSERVATIVE BUREAUCRATS FOLLOW FUKUDA'S ECONOMIC LEADERSHIP. ONLY ITI MIN KOMOTO IS CALLING FOR FURTHER MEASURES TO HELP BUSINESS OUT OF RECESSION, BUT WITHOUT SUCCESS.

4. SUZUKI ARGUES THAT IN VIEW OF PRESENT LARGE UNUTILIZED CAPACITY (WHICH EVEN FUKUDA READILY ADMITS) GOJ OFFICIAL FORECAST AND OBJECTIVE OF ONLY 5.6 PERCENT GROWTH IN REAL GNP JFY 76 IS FAR TOO LOW. WITH CAPACITY GROWING AT MORE THAN 6 PERCENT, GAP BETWEEN ACTUAL AND POTENTIAL WILL WIDEN. IN TERMS OF NEW MEDIUM-TERM PLAN JFY 76-80 UNDER WHICH GNP POTENTIAL IS TO INCREASE AT AVERAGE ANNUAL RATE OF 6.3 PERCENT, ECONOMY'S ACTUAL PERFORMANCE WILL FALL SHORT OF THE OBJECTIVE UNLESS CURRENT POLICY IS DIRECTED TOWARDS CLOSING THE GAP BETWEEN ACTUAL AND POTENTIAL GNP. IN ORDER TO ACHIEVE A "SOFT LANDING" ON POTENTIAL GROWTH RATE, SUZUKI BELIEVES JFY 76 REAL GNP MUST BE ABOUT 7-8 PERCENT.

5. THIS "MORE APPROPRIATE" GROWTH TARGET FOR CURRENT YEAR CAN ONLY BE ACHIEVED THROUGH A FURTHER FISCAL STIMULUS TO ACCELERATE REAL GNP ADVANCE BY 2-3 PERCENTAGE POINTS ABOVE OFFICIAL TARGET OF 5.6 PERCENT FOR JFY 1976. ASSUMING A MULTIPLIER OF 2, THE AMOUNT OF STIMULUS NEEDED WOULD AMOUNT TO ABOUT YEN 1.5-2 TRILLION. IN TERMS OF THE JFY 76 LIMITED OFFICIAL USE

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BUDGET (SEE TOKYO 1629 AND A-118) IT WOULD BE EQUIVALENT TO AN INCREASE IN EXPENDITURES FROM YEN 24.3 TRILLION TO BETWEEN YEN 25.8-26.3 TRILLION. THAT WOULD REPRESENT AN INCREASE OVER LAST YEAR'S REVISED BUDGET EXPENDITURES OF BETWEEN 18.5 PERCENT AND 20.8 PERCENT COMPARED WITH 16.6 PERCENT INCREASE IN BUDGET CURRENTLY BEFORE DIET.

6. SUZUKI BELIEVES THE ADDED FISCAL STIMULUS SHOULD BE

INTRODUCED IMMEDIATELY AND INCLUDE AN INCOME TAX CUT (PROBABLY AN INCREASE IN THE AMOUNT OF PERSONAL EXEMPTIONS) TOTALING YEN 1 TRILLION. THAT SORT OF POLICY RECOMMENDATION HAS POLITICAL APPEAL IN THIS ELECTION YEAR. NEVERTHELESS FINATT BELIEVES THE ECONOMIC REASONING IS SOUND.

7. SUZUKI BELIEVES THAT UNDER CURRENT POLICY, ECONOMIC ADVANCE WILL FALL SHORT OF 5.6 PERCENT FORECAST. THE INCREASE IN REAL GNP MAY ONLY BE 4 PERCENT AND SOME ACADEMIC ECONOMISTS ARE REPORTEDLY PROJECTING EVEN LESS. CONSEQUENTLY THERE IS A SERIOUS DANGER, SUZUKI SAYS, OF JUST STICKING TO PRESENT POLICIES. A SLOW RECOVERY WILL PREVENT JAPAN FROM MEETING CURRENT POLICY OBJECTIVES OF (1) PRICE STABILITY, (2) REDUCTION IN UNUTILIZED CAPACITY, AND (3) REDUCTION IN UNEMPLOYMENT. THE PROFIT SQUEEZE ON BUSINESS WILL CONTINUE, LEADING TO PRICE INCREASES AND A FASTER RATE OF INFLATION.

8. THESE VIEWS WERE CONTAINED IN A REPORT ISSUED BY THE "FORUM ON POLICY CONCEPTS" COMPRISING SUZUKI AND 12 OTHER PROMINENT BUT LARGELY ACADEMIC ECONOMISTS, PUBLISHED IN NIHON KEIZAI SHIMBUN OF APR 3 (WHICH WILL BE TRANSMITTED AS SOON AS FULL ENGLISH TRANSLATIONS IS COMPLETED). SUZUKI SAYS RESULTS OF HIS ANALYSIS AND RECOMMENDATIONS ARE CONFIRMED BY INDEPENDENT STUDIES OF OTHER REPUTABLE ECONOMISTS. SOME ARE BASED ON ENTIRELY DIFFERENT ANALYTICAL TECHNIQUES (INCLUDING INPUT-OUTPUT APPROACH USING A TURN-PIKE MODEL).

9. COMMENTS. FINATT SHARES VIEW THAT JFY 76 BUDGET IS NOT VERY STIMULATIVE (SEE TOKYO 1629 AND A-118) AND WILL NOT LIFT ECONOMY OUT OF DOLDRUMS UNLESS PRIVATE SPENDING PICKS UP SUBSTANTIALLY. RECENT DATA (REPORTED IN LIMITED OFFICIAL USE

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WEEKLY FINANCIAL AND ECONOMIC DEVELOPMENTS CABLES) SUGGEST THAT EXPORT DEMAND HAS BEEN FAR STRONGER THAN MOST WOULD HAVE IMAGINED SOME MONTHS AGO AND THAT CONSUMER DEMAND MAY BE REVIVING. IT IS NOT YET CLEAR WHAT DEMAND SECTORS HAVE CAUSED RECENT UNANTICIPATED JUMP IN INDUSTRIAL PRODUCTION AND SHIPMENTS. DESPITE THESE ENCOURAGING SIGNS THAT ECONOMIC REVIVAL IS AGAIN UNDER WAY IN JAPAN, FUKUDA'S PAST POLICIES HAVE ERRED ON THE "DOWN SIDE." ADDED FISCAL STIMULUS RECOMMENDED BY SUZUKI, IF INTRODUCED PROMPTLY, WOULD STRENGTHEN BUSINESS AND CONSUMER PSYCHOLOGY, PREVENTING THE KIND OF STOP-GO FISCAL STIMULI OF LAST YEAR, AND ENSURE THAT RECOVERY WILL BE SELF-SUSTAINING. THERE ARE RISKS THAT STIMULUS COULD BE EXCESSIVE BUT FINATT BELIEVES GOJ HAS SUFFICIENT ADMINISTRATIVE FLEXIBILITY (BY DELAYING PUBLIC WORKS SPENDING, RESTRICT-

ING NEW HOUSING OR EXPORT LOANS) TO PERMIT SOME "FINE
TUNING, LATER THIS YEAR. FINALLY, FINATT AGREES THERE IS
CURRENTLY A RISK OF COST-PUSH INFLATION WHICH WOULD BE MITIGATED BY
STRONG RECOVERY IN PRODUCTIVITY AND PROFITS.

10. TIMING: WHILE IT WOULD BE POLITICALLY USEFUL TO
ANNOUNCE TAX REDUCTIONS BEFORE THE LOWER HOUSE ELECTION,
IT IS NOT LIKELY THAT MEASURE COULD BE ENACTED UNTIL AFTER
ELECTION, WHICH MOST OBSERVERS NOW EXPECT TO TAKE PLACE IN
THE FALL.
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